

UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA

UNITED STATES OF AMERICA, : Civil Action  
: No. 1:11-cv-00948  
Plaintiff, :  
: September 7, 2011  
v. : Afternoon Session  
: Washington, D.C.  
H&R BLOCK, INC., et al., :  
Defendants. :  
.....:

TRANSCRIPT OF PRELIMINARY INJUNCTION HEARING - DAY 2  
BEFORE THE HONORABLE BERYL A. HOWELL  
UNITED STATES DISTRICT COURT JUDGE

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25 Proceedings reported by machine shorthand, transcript  
produced by computer-aided transcription.

I N D E X

<u>WITNESS</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>
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ADAM NEWKIRK				
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E X H I B I T S

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P R O C E E D I N G S

THE COURT: Before we begin with Mr. Newkirk, I just want to alert everybody that the leak that started in my jury room apparently has spread to the reception area of the courtroom, so just if everybody could please be careful when they're walking in and out of the courtroom, that they don't slip. It's the benefits of being in the old building.

Mr. Newkirk, please resume the stand. Please begin.

MR. BUTERMAN: With your permission, your Honor, I'd like to just give Mr. Newkirk a number of the folders which are the exhibits that we're going to be using to obviate the need for me to request permission every time.

THE COURT: Have you shared with Mr. Robertson what those exhibits are?

MR. BUTERMAN: Sure.

MR. ROBERTSON: Yes.

THE COURT: Are you ready to begin?

MR. BUTERMAN: Yes, your Honor.

THE COURT: Let's proceed.

DIRECT EXAMINATION (Resumed)

BY MR. BUTERMAN:

Q Good afternoon, Mr. Newkirk.

A Hi.

Q Mr. Newkirk, one of the folders that I handed to you is labeled GX 217.

1 Do you see that?

2 A Yes.

3 Q Could you open up the folder and pull out the document  
4 that's labeled GX 217.

5 Am I correct, Mr. Newkirk, that in the middle e-mail, you  
6 were writing to Mr. Houseworth and attaching an updated digital  
7 competitor file?

8 A Yes.

9 Q And Mr. Houseworth has a response to you presumably after he  
10 looked at what was contained in that file?

11 A I don't see a response to me.

12 Q Oh, I'm sorry.

13 Now, the digital competitor file that you sent to  
14 Mr. Houseworth, is that what's contained on the following  
15 pages?

16 A Yes.

17 Q The digital competitor file is based on E-file share data,  
18 is it not?

19 A Yes. It's provided by the IRS.

20 Q And that's how H&R Block's digital business was looking at  
21 the digital market?

22 A Are you speaking about the competitors or about the E-file?

23 Q The competitors.

24 A I believe the IRS file comes to us with an indicator as to  
25 whether it's an assisted return or digital return.

1 Q So these figures are digital preparers, correct?

2 A Yes.

3 Q And H&R Block relies upon the IRS E-file data for purposes  
4 of analyzing the competitive landscape of digital?

5 A Jason asked me for the file so I don't know what he wanted  
6 it for.

7 Q And Mr. Houseworth at this time is the head of H&R Block's  
8 digital?

9 A He is right now.

10 Q If you'd look at the share figures that are listed at the  
11 top of the document, do you see those?

12 A Yes.

13 Q And you see there's a figure of 62.2 percent for TurboTax, a  
14 figure of 15.6 percent for H&R Block, a figure of 12.8 percent  
15 for TaxACT?

16 Do you see those figures?

17 A Yes.

18 Q And those are the same figures that are contained in the pie  
19 chart to the left, are they not? 15.6 percent for H&R Block,  
20 12.8 percent for TaxACT, 62.2 percent for Intuit?

21 A Yes.

22 Q And if you look at the list of rankings down below, the  
23 share numbers, is it true that after you get past No. 5, no  
24 company has more than .5 percent of the digital market?

25 A No. 6 is .5 percent and it gets lower from there.

1 Q And in fact, if you look at the actual sum total of -- I'm  
2 sorry; let me back up.

3 If you flip to the next page of the document, does that  
4 indicate to you the number of returns that were filed using  
5 each product?

6 A Yes. This is actually even a summary of the data we  
7 received. And it's just an Excel format to get it like this.

8 Q And looking at that, isn't it true that it looks like more  
9 than half of the people or the companies were authorized to file  
10 returns did not file any returns?

11 I mean, there are lots of no numbers next to a bulk of the  
12 companies; isn't that true?

13 A Well, this file has several years in it so those names  
14 probably had returns for other years. They may have changed  
15 their name. I don't know why they disappear from the list.

16 Q Now, Mr. Newkirk, you've been in the courtroom and you've  
17 heard a lot of testimony about migration between assisted and  
18 digital over recent years at H&R Block, correct?

19 A Correct.

20 Q Year over year, has the migration been relatively flat in  
21 terms of the net -- to use the term of Mr. Bennett, "net-net"?

22 A Between Block retail and Block digital, yes, I believe that  
23 net-net number is pretty consistent.

24 Q And that's despite changes to the nature of the digital  
25 marketplace, correct?

1 A I'm not sure what that means, but my statement is still  
2 that, yes, it's maintained.

3 Q Well, let me ask you: You were involved in 2010, were you  
4 not, in an effort to convince H&R Block to market free more  
5 prominently on the digital side?

6 A I was asked to provide an analysis of our free product.

7 Q Let me make sure I'm clear. Were you or were you not part  
8 of a group of people who were promoting an idea to H&R Block  
9 executives that H&R Block should be comfortable marketing free  
10 aggressively?

11 A I'm not sure if I was a part of a particular group.

12 Q Okay. Could you look at what's been marked as GX 812.

13 Mr. Newkirk, do you recognize GX 812 as an e-mail from Laura  
14 VanGoethem to several others, copying you and Heather Watts?

15 A I see it, although I don't particularly remember this exact  
16 e-mail.

17 Q You see at the top of the e-mail, it says, "Hey, guys,  
18 Heather, Adam and I just met and feel comfortable with the  
19 below"?

20 A Yes.

21 Q And the Adam that's being referred to there is you?

22 A I would assume so, yes.

23 Q And do you see that the proposal that's contained in this  
24 e-mail is to communicate free across all media channels?

25 A Yes.



1 Q And do you see that -- if you look at the -- if you look at  
2 the last paragraph on the page, it says, "Simple enough until  
3 the reality of our franchisees creep in."

4 Do you see that?

5 A Yes.

6 Q And the e-mail goes on to say, "We need to educate them on  
7 the true risk (which is very low, see below) to their business."

8 Do you see that?

9 A Yes.

10 Q And then it goes on to say, "We believe we should educate  
11 them now."

12 Do you see that?

13 A Yes.

14 Q And then the third bullet point there, it says, "DIYers are  
15 different clients; they are unlikely to move across channels."

16 Do you see that?

17 A Yes, I do.

18 Q Now, H&R Block did ultimately decide to increase its free --  
19 how aggressively it was advertising its free digital product,  
20 correct?

21 A I believe they were more aggressive in '10 than '09.

22 Q And despite becoming more aggressive in free, the  
23 year-over-year migration from retail to digital was totally  
24 unchanged, correct?

25 A It appears like the net number didn't change a lot. I think

1 that's all that's represented here.

2 Q Okay. Let me have you look at GX 813.

3 And do you see your e-mail to Mr. Houseworth and Mr. Hoffman  
4 copying Mary Haring from September 16th, 2010?

5 A Yes.

6 Q And in the e-mail, you say, "You are correct regarding free  
7 cannibalization. We have not seen increased migration from  
8 retail as we launched free and subsequently became much more  
9 aggressive in free last year. YOY" -- that's year over year?

10 A Yes.

11 Q "Year-over-year migration from retail to digital as a  
12 percent of retail clients was totally unchanged last year,  
13 2.2 percent. On the side note, digital-to-retail migration was  
14 also unchanged last year, 4.4 percent."

15 Do you see that?

16 A Yes.

17 Q Okay. So just so we're clear, despite the fact that  
18 H&R Block began more heavily promoting its free product in  
19 digital, the year-over-year migration between digital and retail  
20 did not change, correct?

21 A I'm not sure when they started marketing what, but I  
22 definitely agree that the year-over-year migration didn't  
23 change.

24 Q And by the way, when we're talking about these figures, I  
25 see 2.2 percent and 4.4 percent. We're not talking about a lot

1 of customers anyway, are we?

2 The numbers are roughly a couple hundred thousand,  
3 correct?

4 A I think it's around 300,000, yes.

5 Q Mr. Newkirk, do you know what the Ninja is?

6 A Yes.

7 Q Could you tell the Court what the Ninja is.

8 A It's a file that's primarily used to show forecast changes  
9 so it has lots of information about the P&L, about average  
10 revenue per unit.

11 Q In fact, it's a document that contains various analyses  
12 of -- or breakdowns of H&R Block's products and sales margins  
13 and things of that sort?

14 A That's a pretty good description.

15 Q And its finances?

16 A Yes.

17 MR. BUTERMAN: Okay. Your Honor, the Ninja is the  
18 document that I think both sides believe is a confidential  
19 document. It contains confidential business information. And  
20 at this time, we would request that the courtroom be sealed so  
21 that I could ask Mr. Newkirk some questions regarding the  
22 numbers contained in the Ninja.

23 THE COURT: Okay. Will everybody in the spectator  
24 seats, unless they are associated with one side or the other,  
25 please leave. How long do you expect this to be?

1 MR. BUTERMAN: Not more than 10 or 15 minutes, your  
2 Honor.

3 THE COURT: Then just for spectators, it's probably  
4 going to be 10 or 15 minutes, and then we're going to probably  
5 cover part of this on redirect initially.

6 MR. ROBERTSON: Yes, your Honor.

7 THE COURT: So I don't know how long it will be.  
8 Between 20 to 30 minutes the courtroom will be closed, and this  
9 portion of the record will be sealed.

10 MR. BUTERMAN: Thank you, your Honor.

11 THE COURT: I'll invite everybody to leave who doesn't  
12 have to be here.

13 MR. ROBERTSON: Make sure we're clear here, what  
14 counsel is doing is he is going to do whatever is confidential,  
15 and then I can go into my redirect.

16 THE COURT: That was my anticipation in the  
17 clustering.

18 MR. ROBERTSON: That's what mine was too.

19 (The following portions, pages 13-41, were designated as  
20 confidential/attorneys' eyes only and sealed under a  
21 separate transcript per order of the Court.)  
22  
23  
24  
25

1 THE COURT: Mr. Robertson, whenever you're prepared to  
2 proceed with your cross-examination.

3 MR. ROBERTSON: Yes, your Honor. I was just checking  
4 to see where Mr. Dunn was so we weren't missing anyone in action  
5 there because I think he goes next.

6 CROSS-EXAMINATION

7 BY MR. ROBERTSON:

8 Q Sir, now we can ask you some questions that are not in the  
9 super confidential part of the record, and so that's where I'd  
10 like to stay if you can bear with me, okay?

11 A Okay.

12 Q I don't think it's a secret. Do you know whether you're an  
13 executive at H&R Block?

14 A I wouldn't consider myself an executive.

15 Q And do you know what the term "C level manager" is at H&R  
16 Block?

17 A Yes.

18 Q What's that?

19 A It means their manager starts with a "C" like CFO and CEO.

20 Q Have you ever provided any reporting to Mr. Cobb, the CEO  
21 currently, that you know of?

22 A Not directly. I would assume some of the things I give to  
23 Jason have been passed on.

24 Q But you don't know?

25 A I don't know.

1 Q And counsel asked you about pricing. Do you have any  
2 decision-making authority at all in terms of pricing within  
3 digital?

4 A No.

5 Q Anywhere in the company?

6 A No.

7 Q Do you have any decision-making authority at all in  
8 marketing of the products?

9 A No.

10 Q Do you actually in your job or your job during the entire  
11 time you've been there, actually been responsible for any aspect  
12 of marketing?

13 A No.

14 Q And back in the fall of 2009, you mentioned the phrase  
15 "decision support."

16 What was decision support?

17 A My primary job was doing budgeting and forecasting for the  
18 digital business. Predicting revenues and expenses based on the  
19 assumptions given to me by management.

20 Q Okay. And did you have any decision-making role in terms of  
21 this acquisition?

22 A No.

23 Q Back in 2009, did anybody ever tell you what the purpose of  
24 the deal was?

25 A I don't believe so.

1 Q And do you know -- what part of the business, if you know,  
2 did Mr. Schell work in?

3 A He was primarily focused on the assisted side of the  
4 business.

5 Q Okay. Do you know if he was a decisionmaker involved in  
6 the deal?

7 A I don't believe he was.

8 Q And how is it that he was your interim boss? You used the  
9 word "interim."

10 A John Kill was my supervisor and for a time, I don't think  
11 they knew exactly where I should be in the organization, so I  
12 reported to Brian until they figured that out.

13 Q Okay. And when did they finally figure that out?

14 A I reported to Dennis Armstrong, who was a director primarily  
15 focused on the retail business.

16 Q And then when did you finally start reporting to somebody  
17 over on the digital side?

18 A Just very recently. I started reporting directly into the  
19 digital organization.

20 Q Now, sir, you mentioned that you first got involved in -- or  
21 were asked to work on the reporting back in 2009.

22 Do you know when about in September that was? You said  
23 September.

24 A I might have first heard about it in August. I don't think  
25 I was asked to do anything until September.

1 Q And you mentioned when you first asked to work on it, then  
2 you went on vacation for about a week?

3 A Yes.

4 Q And counsel showed you a model that you had been given to  
5 put numbers in.

6 Do you remember that, sir?

7 A Yes.

8 Q And after you did that, did you ever see that model again?

9 A No. When I returned from vacation, Tony Bowen had created a  
10 new model that he asked me to update from there on forward.

11 Q And did you do that?

12 A I did.

13 Q And then did there come a point in time that you had any  
14 understanding as to whether the deal was going to go forward  
15 in 2009?

16 A I would routinely follow up with Tony to ask out of  
17 curiosity how it was going. And at some point, he said the deal  
18 was dead.

19 Q Okay. And when about did that happen; do you remember?

20 A I don't remember.

21 Q And do you know who Mr. Hoffman is, William Hoffman?

22 A Yes.

23 Q Who is he, sir?

24 A He is now a director in accounting, but most of the time  
25 I've worked with him he's either been a manager -- he is a



1 manager in finance.

2 Q Did he have any authority to set prices over in digital, if  
3 you know?

4 A No, he didn't.

5 Q And counsel was asking you about going free at Block, and  
6 you gave your views on that.

7 Without going into the nitty-gritty numbers of that, can you  
8 just explain to the Court why you believed it was a good thing  
9 for Block.

10 A Well, it was based on the numbers, the amount of incremental  
11 new client growth that I was seeing through that product.

12 Q And can you explain why that's good.

13 A Generally, more clients means more money.

14 Q And in that case, were you able to determine whether more  
15 clients meant more money?

16 A We certainly make a huge percentage of our revenue from our  
17 clients who start free.

18 Q Later in 2010, did there come a point in time when they  
19 asked you to continue to write reports for the company relating  
20 to TaxACT?

21 A Yes.

22 Q About when did that happen, sir?

23 A I believe it was around July.

24 Q Of what year? 2010?

25 A 2010, yes.

1 Q And at that time, did anybody tell you what the purpose of  
2 the deal was?

3 A I don't know.

4 Q Did you ever have any role at all in making any decision  
5 regarding this transaction?

6 A Decision making?

7 Q Yes, sir.

8 A Definitely not.

9 MR. ROBERTSON: Okay. Your Honor, may I have a quick  
10 moment?

11 THE COURT: Yes, you may.

12 (Brief pause.)

13 MR. ROBERTSON: Your Honor, I don't have any more  
14 questions at this time.

15 THE COURT: Sure.

16 Mr. Buterman, any redirect?

17 MR. BUTERMAN: Yes, your Honor. May I proceed?

18 THE COURT: Yes, please.

19 MR. BUTERMAN: Thank you.

20 REDIRECT EXAMINATION

21 BY MR. BUTERMAN:

22 Q Mr. Newkirk, you're routinely asked to keep track of  
23 TaxACT's prices, are you not?

24 A I've been asked that from time to time.

25 Q And isn't it a fact that except when asked to do so by the

1 lawyers in this investigation, you have not been asked to track  
2 the pricing information for any firms other than Intuit and  
3 TaxACT?

4 MR. ROBERTSON: Objection; beyond the scope.

5 THE COURT: I'll allow it. You may answer the  
6 question.

7 BY THE WITNESS:

8 A Me personally?

9 Q Yes, you.

10 A No, I don't recall.

11 MR. BUTERMAN: No further questions, your Honor.

12 THE COURT: Would you like to question?

13 MR. ROBERTSON: No, your Honor.

14 THE COURT: Mr. Newkirk, you're excused.

15 (Witness exits the courtroom.)

16 THE COURT: I think before you call your next witness,  
17 we'll take a short break to give my court reporter a chance to  
18 rest her fingers before we get to the next witness, so we'll  
19 take a ten-minute break.

20 (Recess was taken.)

21 THE COURT: Is the government ready to call its next  
22 witness?

23 MR. WAYLAND: We are, your Honor. We call Lance Dunn  
24 to the stand.

25 (WHEREUPON, the witness was sworn.)

1 LANCE DUNN,  
2 called as a witness herein, having been first duly sworn, was  
3 examined and testified as follows:

4 MR. WAYLAND: May I proceed, your Honor?

5 THE COURT: Yes, please.

6 DIRECT EXAMINATION

7 BY MR. WAYLAND:

8 Q Good afternoon, Mr. Dunn. We've met before. You were here  
9 for the opening yesterday?

10 A Yes.

11 Q All right. So you know who I am then. Let's find out who  
12 you are. You're the president and cofounder of 2nd Story  
13 Software?

14 A Yes.

15 Q And 2nd Story is the maker of TaxACT?

16 A Yes.

17 Q It was founded in 1998?

18 A Yes.

19 Q And prior to founding 2nd Story, you were employed by  
20 Parsons Technology?

21 A Yes.

22 Q What was Parsons Technology?

23 A Parsons Technology was a provider of consumer software.  
24 They sold direct to consumers. Had a catalog of approximately  
25 75 products, mostly in financial and productivity. Although

1 they had some in the religious product line as well.

2 And Parsons, you know, was a direct-to-consumer tax -- or  
3 software company including the tax software, but they were a  
4 direct-to-consumer software company that sold through direct  
5 mailing catalogs.

6 Q And they had a digital tax preparation product called  
7 "Personal Tax Edge"; is that correct?

8 A Yes, they did.

9 Q Did you work on that product?

10 A Yes, I did.

11 Q What's your training, background? Are you A programmer?  
12 Are you a tax person?

13 A I have a Bachelor of Arts in accounting from Coe College in  
14 Cedar Rapids, Iowa. And I passed the CPA shortly after  
15 graduating.

16 Q Did you develop the software for the product or were you  
17 more the what you need to do and have somebody else convert it  
18 into software?

19 A You know, it's really a gray line between programming and --  
20 I provided content for that product. Using third-generational  
21 software development tools, I would say I actually did and do a  
22 lot of programming.

23 Q You still do that?

24 A Not today.

25 Q At the time you worked there, was the Personal Tax Edge

1 product in the market being sold?

2 A Yes.

3 Q Okay. And who was its closest competitor?

4 A You know, there were really only two other software products  
5 in the market at the time, which was TurboTax and Block,  
6 although, you know, we really competed with everybody even then,  
7 with everything.

8 The tax market -- tax preparation market -- even back in '91  
9 when I started at Parsons, you know, Parsons sent their mailings  
10 out to as many people as possible.

11 Q In 1994, Intuit acquired Parsons, correct?

12 A Yes.

13 Q After acquiring Parsons, what did Intuit do with Personal  
14 Tax Edge?

15 A They continued to run the product as is for about two years.  
16 And then they discontinued the product and merged it in with  
17 their pro series and TurboTax product lines.

18 Q And after Intuit discontinued the product, what did you  
19 do?

20 A I continued at Parsons Technology as vice president of  
21 software development overseeing the development efforts of  
22 approximately 30 internally developed applications, as well as  
23 20 externally licensed.

24 Q Did you leave Parsons eventually?

25 A Yes. Parsons went through a succession of owners. After

1 Intuit, it was owned by Broderbund. And four of us left Parsons  
2 in February of 1998 to start 2nd Story Software.

3 Q And what was the purpose of starting 2nd Story Software?  
4 What was your business objective?

5 A Our business objective was to make money selling value tax  
6 software which, you know, was a category that did not exist at  
7 that time.

8 Q Well, you created a new category?

9 A We recreated it. It was the niche that the Personal Tax  
10 Edge product line filled when it existed.

11 Q At the time you started -- since that product had already  
12 been discontinued then, you were starting a new niche in your  
13 mind, right?

14 A Yes. We were also, you know, utilizing -- a lot of what we  
15 were, as much as what we were not, was as a result of our  
16 Parsons experience. And we absolutely set out to do things  
17 differently than how we did them at Parsons. While we had seen  
18 a lot of efficiencies in how we did things there, we really felt  
19 that we could do things even much more efficiently on our own  
20 with 2nd Story. In particular, with how we market, distribute  
21 and support the product in using the Internet as opposed to  
22 telephone and direct mail pieces.

23 And we created a development environment that was just far  
24 more efficient utilizing rapid development and short feedback  
25 loops.

1 Q When you started 2nd Story, what were the principal  
2 competitors in the digital software product market?

3 A In digital software, there was only two other companies that  
4 provided software products at that time, TurboTax and Block's  
5 TaxCut at that time.

6 Q You founded TaxACT to provide a high-quality product at a  
7 reasonable price, right?

8 A Absolutely.

9 Q And you've been pretty successful at that?

10 A I'm happy with the success that we've had.

11 Q And you attribute the success to your business model of  
12 providing a high-quality product at a reasonable price?

13 A Yes. The high-quality product at a reasonable price is a  
14 driver of the value model that we employ at 2nd Story  
15 Software.

16 Q And I think you frequently have described your TaxACT effort  
17 as a pioneer, correct?

18 A We have, yes.

19 Q Pioneer in providing free online tax preparation software  
20 and electronic filing services, correct?

21 A Yes. Even in 1998, we provided a free product drawing upon  
22 our experience with free products at Parsons. So our initial  
23 product offering in 1998 was a free federal program, free to  
24 prepare, free to print.

25 Q So your product model, essentially, was you'd be aggressive



1 in marketing free to attract people in the door and then upsell  
2 them into your product that you were selling, right?

3 A At that time, it really was just to get our product in front  
4 of as many people as possible. But yeah, the plan was the model  
5 at that time -- in 1998, the model was to provide a free federal  
6 program that was free to prepare, free to print.

7 If you wanted to E-file, there was an additional charge for  
8 that and if you needed a state program, there was an additional  
9 charge for that. In 1998, we had 23 state programs. Far from  
10 complete.

11 Q And over the years, as you developed your strategy, you  
12 focused on free as being your tag line; getting people in the  
13 door with the free provide and then provide them with a  
14 high-quality, low-cost upgrade?

15 A Right. Free is an integral part of the value model. And  
16 the beauty of it is it has universal appeal. Everybody likes  
17 something for free.

18 Q You've been an industry leader in helping the IRS achieve  
19 key milestones in its objective of having 70 percent of  
20 individuals file tax returns electronically, right?

21 A Yes. By certainly over the years by giving away free  
22 product and eventually giving away free E-filing, that I'm sure  
23 has helped the IRS.

24 Q You have described your company as a maverick, right?

25 A We have. I'm not sure that the context that I used it in is

1 the same that you are today, but we have used maverick in a  
2 press release before.

3 Q You have described -- you -- let me ask you before we get  
4 much further in this, Mr. Dunn, because I think it will help us  
5 set the stage for the rest of the afternoon.

6 You have, in your mind, a distinction between a value and a  
7 premium market, don't you?

8 A Yes.

9 Q And you think that you compete in the quote, "value market,"  
10 right?

11 A Yes, I do.

12 Q And some other people compete into the premium market?

13 A Yes. And at this point, you're speaking specifically of tax  
14 software; that there's a value in premium distinction within tax  
15 software, yes.

16 Q What about online?

17 A Same categories.

18 Q Okay. Let's use digital to refer to both software and  
19 online. If you think your answer requires a distinction, you  
20 let me know, okay?

21 A Okay.

22 Q So we'll go to digital.

23 And you believe there's a value market and a premium market,  
24 right?

25 A Yes.

1 Q You quite firmly believe that?

2 A Yes.

3 Q And you compete in the value market, right?

4 A Yes.

5 Q I'm going to go to the board next to you, with the Court's  
6 permission, and I'm going to do a little writing and then you  
7 can help me out, okay?

8 MR. WAYLAND: Your Honor, may I approach the board?

9 THE COURT: Yes, please.

10 BY MR. WAYLAND:

11 Q All right. Mr. Dunn, I have approached the board, and on  
12 the left side I'm going to write the word "premium." I'm  
13 drawing a line down the middle. And on the right side, I'm  
14 going to write the word "value." And then we're going to write  
15 the word "digital" across the top because we're agreed, at least  
16 for now, to talk about the market like that.

17 Now, on the value side, tell me, you're on there, right,  
18 TaxACT?

19 A TaxACT would be a value company, yes.

20 Q Okay. TaxACT. And any others?

21 A Free Tax USA, TaxSlayer.

22 Q Free Tax, TaxSlayer. Anybody else?

23 A There are others.

24 Q Anybody serious? Anybody you really care about a lot?

25 A You know, we watch them all. Free Tax USA and TaxSlayer are

1 the two that have adopted the free -- have adopted the value  
2 model the best.

3 Q How about TaxHawk?

4 A TaxHawk and Free Tax USA are the same company. Free Tax USA  
5 represents like 18 different Web sites. That's why it's  
6 difficult to say who is who.

7 Q So these are the top guys, and then there's maybe 20 or so  
8 more that at least pretend to be in the business?

9 A There are some other software companies, yes, that could be  
10 in the value segment.

11 Q But nobody you think we need to put on the chart right now  
12 to think about serious competitors?

13 A No.

14 Q All right. On the premium side, who is on the premium  
15 side?

16 A CCH, Wolters Kluwer, with a product called "Complete Tax."  
17 You'd have Liberty Tax with their eSmart Tax. You'd have  
18 Jackson Hewitt licenses a copy of CCH. But they are also in the  
19 premium Space. Intuit, Block. Fileyourtaxes.com.

20 Are you asking me to repeat the list of the FFA Web site  
21 from memory?

22 Q No. I'm asking you to tell me who you think is in the  
23 premium market, sir. If you think there are -- well, let's just  
24 get your list and then we'll -- obviously, you didn't give me  
25 everybody who is on the Free File Alliance.

1 A Fileyourtaxes.com.

2 Q We'll call them "FYT," okay.

3 A Let's see who else is on the FFA Web site. Those are  
4 some --

5 Q Do you have an idea in the premium market what share Intuit  
6 and Block represent?

7 A Well, by revenue, Intuit is 80 percent of all software, all  
8 by themselves. I think they did \$1.3 billion in consumer  
9 software last year.

10 Q Okay. And what about Block? 80 percent for Intuit. What  
11 percent for Block; do you think?

12 A Block probably did 200 million. So they're probably less  
13 than 10 percent.

14 Q And the rest of these, it splits up for the other  
15 10 percent somewhere, do you think, in the premium side?

16 A No. Intuit 80 percent. That's all software. That is  
17 across the board.

18 Q Well, I'm trying to focus today on the digital market.  
19 Premium digital market, you've identified Intuit and Block as  
20 competitors.

21 You may not know, but if you do know, tell me what  
22 percentage of the premium digital market Intuit has.

23 A I don't know.

24 Q Do you have any guess? Do you ever think about it?

25 A No.

1 Q Okay. And Block, you don't know what their percentage is  
2 either, sir?

3 A No.

4 Q And what about on the value side? Do you have any idea of  
5 the market shares on the value side of this chart?

6 A No. No one releases those numbers publicly. Where would I  
7 get the information?

8 Q I don't know, sir, but we're going to look at a lot of  
9 documents where you've calculated some market shares, so I was  
10 hoping you'd know something about that.

11 A I've calculated market shares on publicly available  
12 information.

13 Q And sitting here today, you don't remember what kind of  
14 numbers you've been using?

15 A You know, I believe we have calculated them for using the  
16 publicly reported units of like Intuit and block.

17 Q Let me ask you this: You're the CEO of the company today,  
18 right?

19 A Yes.

20 Q What are your market shares in the market that you've just  
21 described to the Court?

22 A What market did I describe to the Court?

23 Q I asked you -- the value digital market. You said you  
24 compete in the value digital market, okay?

25 A That's true.

1 Q Do you compete in a different market?

2 A Well, we compete in the market for tax preparation, yes.

3 Q All right.

4 A We compete for 140 million taxpayers. There's 140 million  
5 different reasons why somebody selects any of these.

6 Q All right, sir. But focusing ourselves on the value,  
7 digital -- if you don't want to use the market, we'll use  
8 something else -- but the digital value segment of whatever it  
9 is you're talking about, do you have any idea of what your share  
10 is within that segment?

11 A Between TaxACT, Free Tax USA and TaxSlayer, no. TaxACT,  
12 Free Tax USA and TaxSlayer do not publicly announce their  
13 numbers.

14 Q So you're sitting at a board meeting and somebody says  
15 what's the share of your market, what do you say?

16 A If there's an analysis done, we would compare E-files, which  
17 is released publicly. So for example, the IRS announces how  
18 many E-files are done across the entire tax preparation industry  
19 and how many E-files are done as DIY.

20 So in the board context, we would say, okay, here's the  
21 number of federally accepted E-files divided by the total in DIY  
22 software, and here's the number of E-files we have across all  
23 tax preparation.

24 Q Okay. And the last time somebody at the board asked you  
25 that, what did you say? What numbers did you give them?

1 A In terms of --

2 Q Market share.

3 A Yes.

4 Q You're sitting at a board meeting.

5 A Let me answer, please.

6 Q I'm trying to get you to answer my question. That's what  
7 the purpose is here, okay. If you can't answer the question,  
8 just tell me and I'll help you out.

9 My question is: The board is sitting --

10 MR. ROBERTSON: Objection. Can we have counsel slow  
11 down.

12 MR. WAYLAND: Sure. I'll slow down.

13 THE COURT: Mr. Dunn, please respond and answer the  
14 questions. And if you have to provide a caveat to your answer  
15 in order to answer it as accurately as you feel comfortable  
16 answering, please do so. But we're wasting a lot of time here  
17 going back and forth.

18 So could we answer the question. If you want to answer  
19 the question about market share based on E-filings and DIY  
20 software, please do so as promptly and quickly as possible  
21 because we've now spent five minutes go round and round and not  
22 gotten an answer to a fairly simple question.

23 BY THE WITNESS:

24 A The share of TaxACT's DIY software would be about  
25 12 percent.



1 Q And what are you counting when you say 12 percent? Just  
2 this market or premium value?

3 A That would be TaxACT's consumer E-files divided by all DIY  
4 E-files, do-it-yourself.

5 Q You're including pen and paper?

6 A No. It would include all -- Free File Alliance. It would  
7 include fillable forms on the Free File Alliance. It would  
8 include all value, all premium. All DIY solutions.

9 Q And when you're looking at DIY solutions, you then are  
10 including the firms on this (indicating) side of the line,  
11 correct?

12 A That is the publicly available information we can use. We  
13 would also share -- compute our market share as a percentage of  
14 the total; that is, all consumer E-filed returns. That includes  
15 assisted prep regardless of their source.

16 Q And what you don't do is calculate your percentage of the  
17 value side, as you've identified it, correct?

18 A I don't have the information to compute that.

19 Q Okay. Now, sir, do you compete across this (indicating)  
20 line at all? Do you consider yourself in competition with  
21 anybody on the left side of the line?

22 A I compete with everybody in tax preparation, yes.

23 Q So the answer is yes, you are competing across this line  
24 (indicating), correct?

25 A I compete with all of those people. I compete with every

1 CPA. I compete with every enrolled agent. I compete with  
2 wherever 140 million taxpayers get their tax return done.

3 MR. WAYLAND: Okay. Your Honor, I'm just marking this  
4 as Trial Exhibit 5.

5 (WHEREUPON, a certain document was marked Trial Exhibit 5  
6 for identification as of September 7, 2011.)

7 BY MR. WAYLAND:

8 Q All right, sir. You are proud enough of your business that  
9 you're willing to sign your name on a letter out to the public,  
10 right, describing the business?

11 A Yes.

12 Q All right. Let's take a look at Government Exhibit 28.

13 MR. WAYLAND: Your Honor, we have binders to hand to  
14 the witness and the Court, if you want one.

15 THE COURT: Yes, please.

16 BY THE WITNESS:

17 A What document am I looking at?

18 Q I haven't told you yet. Just wait a second. It's  
19 Government Exhibit 28. It is at Tab 3.

20 Mr. Dunn, this is a document that begins with the page  
21 "TaxACT, Your Affordable Solution for Tax Software." And then  
22 it continues on and ends before the back page with a letter  
23 signed by you or a note from the president.

24 Do you see that? It's on page 19.

25 A Yes.

1 Q Do you recognize this document?

2 A Yes. This is a press kit.

3 Q What was the purpose of a press kit?

4 A A press kit is to provide information to media so that they  
5 will include us in reviews, articles, news stories.

6 Q And you don't want to mislead the press, right?

7 A No.

8 Q Everything in here is accurate, as far as you know?

9 A Yes.

10 Q All right. Let's look at a couple of pages in here.

11 Let's go right to your letter because I think that's  
12 actually pretty good. That's at the end of the document. It's  
13 on page 18.

14 Do you have the letter in front of you?

15 A Yes.

16 Q And you signed the letter, right? You wanted people to know  
17 that you stand behind the company and what you say about it?

18 A Yes.

19 Q All right. And so you say at the top, second sentence,  
20 "Since that time," meaning 1998, "TaxACT has been a catalyst for  
21 change in the tax preparation industry."

22 And that's true, correct?

23 A Yes.

24 Q And you're very proud of it because TaxACT was the first  
25 service to offer free preparation of federal taxes, correct?

1 Is that right?

2 A We weren't exactly the first, but yes, we're claiming that  
3 here.

4 Q And you're claiming it because you were a leader in that at  
5 least, right?

6 A Yes.

7 Q You were aggressive. You are the first one to be aggressive  
8 about it, right?

9 A Yes.

10 Q And then you were the first to offer free printing of a  
11 federal tax return, correct?

12 A Yes.

13 Q And the first to offer free E-filing of a federal tax  
14 return?

15 A We offered it at the same time as everybody else did in the  
16 FFA, but I think the point here is we were the first to offer  
17 free for everyone in 2003.

18 Q And at that time, other providers were just offering it free  
19 depending on income level?

20 A On the FFA?

21 Q Or in 2003. What made you different in 2003?

22 A In 2003, we made a very broad-based offer on the Free File  
23 Alliance that was different from the competitors. At that  
24 point, the other products listed on that page would not have had  
25 an offer as broad as ours.

1 Q And in summary, you made sure that TaxACT has consistently  
2 forced the tax preparation industry to become more competitive.

3 That's your true, right, and continues to be your view  
4 today?

5 A Yes.

6 Q And in doing so, you forced your competitors to change as  
7 well, correct?

8 A It's a pretty broad statement. The objective of this  
9 document is to, you know, set us apart and try and get us  
10 included into, you know, articles and news stories when they  
11 might not have otherwise included us.

12 So yes, we were trying to show that we were unique.

13 Q But, this isn't very different than the story you generally  
14 tell about the company, is it?

15 A No.

16 Q If you would go back a page to page 17 -- 16 and 17.

17 MR. WAYLAND: Can we put them both up.

18 BY MR. WAYLAND:

19 Q You'll see here, Mr. Dunn, that you have listed -- you have  
20 there two charts, and one is on the left side entitled "Entry  
21 Level Standard Software Comparison Chart."

22 Do you see that?

23 A Yes.

24 Q On the right side, you have "Deluxe/Premium Software  
25 Comparison Chart," right?

1 A Yes.

2 Q And then underneath the left-hand side, you've listed three  
3 competitors, TaxACT TurboTax and TaxCut, correct?

4 A Yes.

5 Q And on the right side, you've listed the same three  
6 competitors, correct?

7 A Yes.

8 Q This chart doesn't look very much like that chart we made on  
9 the board over there (indicating), does it?

10 A The TurboTax --

11 Q Yes or no? Just yes or no?

12 A No.

13 Q Okay. And you have your company, TaxACT, listed under a  
14 column that says "Deluxe/Premium," right?

15 A Yes. That is the name of our product that's included in  
16 that program, Deluxe. And Premium is the name of the TaxCut  
17 product included in that column.

18 Q Okay. And let's go back to page 15, one more page back.  
19 There's a pie chart at the top and then some Web traffic  
20 underneath.

21 Now, Mr. Dunn, do you understand what information is being  
22 conveyed in this with this pie chart? What's Web traffic?

23 A This is using a third-party report from a company called  
24 "Hitwise" that reports by their measurement the amount of  
25 traffic going to tax-related sites.

1 Q Why do you think that would be relevant to the press?

2 A Because we needed to show that we were relevant in the  
3 market. The press generally only covered what they considered  
4 to be the two dominant players, TurboTax and Block. So in order  
5 for us to get coverage, in order for us to get some  
6 representation in those articles because our product was  
7 different, we needed to show why they should include us.

8 Q All right, sir. And you didn't think you needed to  
9 distinguish yourself from Jackson Hewitt in the chart, right?

10 A In 2008, I don't believe Jackson Hewitt had a software  
11 product.

12 Q But they had an in-store product, didn't they?

13 A This was directed at people that would be creating news  
14 stories about software.

15 Q All right. And there's not really much of a story about you  
16 and Jackson Hewitt with respect to their retail business, is  
17 there?

18 A Not that anyone would write about.

19 Q All right. If you would go to -- well, not yet.

20 Now, on the left-hand side of the chart, we have Block and  
21 Intuit. And you think that both of those companies offer a  
22 premium product, right?

23 A Yes.

24 Q All right. And a premium product, they are able to offer it  
25 partly because they have brand power; is that your view?

1 A Premium is a business model and brand plays into that.

2 Q How does brand played into that?

3 A You know, the distinctions between value and premium is how  
4 you attract customers, how you utilize free, and how you  
5 distinguish yourself, I guess, to the potential customer. A  
6 value product or a value company is going to make price a  
7 primary determinant and have their price prominently displayed.

8 We're also going to use free software to attract as many  
9 people as possible. And we don't care if they use free for  
10 multiple years. We don't care if they use free for one year.  
11 We want them just to keep coming back because that free customer  
12 starts the chain reaction of word-of-mouth advertising.

13 So we utilize free to bring people in, to provide them a  
14 high-quality service, and we hope that they come back. And we  
15 hope they come back as free. When they make the decision to  
16 upgrade to a paid product, it needs to be the customer's choice.  
17 They need to see the value proposition of the product that  
18 they're selecting, whether that's Deluxe, whether that's state.

19 We need to establish a relationship with that customer, and  
20 it has to be based on delivering a high-value, high-quality  
21 product where they have not only the perception of value, but  
22 value in fact.

23 So we utilize free -- when we have free customers, we look  
24 at them as an asset. Free customers are the most likely to come  
25 in, utilize the product and then go around and tell their



1 friends, neighbors and coworkers what a tremendous value and  
2 what a tremendous customer experience they had at TaxACT. A  
3 premium company, on the other hand, utilizes free to attract  
4 customers, but then does everything they can to avoid providing  
5 it.

6 So if you look at some of the, like, Intuits, yes, they'll  
7 advertise free. You'll go to their home page. Free will be  
8 there, but it won't be the default selection. On a value  
9 product, you go to our home page, you go to TaxHawk, you go to  
10 TaxSlayer, free is prominent. And that distinguishes the  
11 difference. That's one of the distinguishing characteristics  
12 between value companies and premium companies, how we utilize  
13 free.

14 Q I don't mean to interrupt you, but you've gone long past  
15 answering my question which is terrific, but just let me pick up  
16 on something.

17 What is the motivation for the Intuits and the Blocks of the  
18 world not to want people to really use their free product?

19 A They're using free because it has universal appeal. They  
20 are putting free out there in front of as many people as  
21 possible to get customers to come to their Web site. Once they  
22 get there, then they're trying to do everything they can to show  
23 that there's reasons why you should use a different product.

24 Q I understand that.

25 A Why the price shouldn't be your primary determinant in

1 making your purchase decision. So yes, brand is part of it.  
2 And they will show the features and they will show the support,  
3 and they will show all the reasons why their paid product is the  
4 appropriate solution for you and not their free product. They  
5 don't depend on word-of-mouth advertising like TaxACT does.

6 Q And they'd rather skip free all together then and just go  
7 right to the higher priced branded product they have, right?

8 A Like I said, they do free because it has universal appeal.  
9 Everyone likes to see a free product. Everyone wants to respond  
10 to free. So when they're casting that net out there to  
11 140 million taxpayers, free has a lot of pull. And they're  
12 getting customers to look at free and come to their Web site and  
13 then evaluate the options that they have.

14 Q And so I understand it, you're doing the same thing?

15 A We also use free because it has universal appeal. But our  
16 free is completely different than, say, the free of Intuit.

17 Q Why do you think your motivation for your free strategy is  
18 different from the motivation that is driving Block and  
19 Intuit?

20 A Our free strategy is what drives 2nd Story Software. We  
21 depend -- our whole life depends on bringing free customers in,  
22 keeping them and having them tell their friends, neighbors and  
23 coworkers about the tremendous value. I can't stand toe to toe  
24 with either Intuit or Block and out-advertise them.

25 Intuit's spent \$1.1 billion last year on sales and

1 marketing; the lion's share of that, I'm sure, on consumer tax.  
2 I spent 25 million. I can't stand there and say, yes, because  
3 my one ad runs once for their 25, you know, that I'm going to be  
4 able to compete with them. I have to utilize free. I have to  
5 provide a great customer service, a great product, and a great  
6 customer experience so that they will tell their friends,  
7 neighbors and coworkers. It's that word-of-mouth chain reaction  
8 that keeps going and keeps perpetuating the growth of 2nd Story  
9 Software.

10 Q Let me see if I can cut to the chase. I think what you're  
11 telling me is that your strategy, as a company, depends on a  
12 robust, free strategy, free product, right?

13 A Yes.

14 Q Okay. And what you're telling me is Block and Intuit don't  
15 have that same strategic imperative to have such a robust, free  
16 product, right?

17 A No. But free is still important to them. I mean, they have  
18 to do free because of the Free File Alliance. Free is not going  
19 anywhere.

20 Q They don't have to do it quite as robustly as you because  
21 your strategy depends on it?

22 A It does today, yes. Now that Intuit and Block are also --  
23 and others are using free products, we do have to differentiate  
24 our free from their free. That's how we attract the true value  
25 customers. And that's how our customers are different than the

1 Block and Intuit customers and other premium customers. Our  
2 customers are value-oriented, price conscious.

3 We make our -- we try to encourage our customers to make  
4 their primary purchase decision based on price. Other products  
5 in the premium -- and you don't have to go any further than look  
6 at these companies' home pages to understand that they are not  
7 making price the primary determinant.

8 Q Now, Mr. Dunn, with the fishing analogy, are you a  
9 fisherman too?

10 A No.

11 Q That seems to be an analogy in the business.

12 MR. WAYLAND: I'm going to have to borrow the  
13 microphone again.

14 BY MR. WAYLAND:

15 Q So I've been thinking about this fishing analogy both you --  
16 both Mr. Bennett and yourself -- I can't do two things at  
17 once -- you and Mr. Bennett have told us about. So let's just  
18 draw a big C down here (indicating).

19 There's a big sea full of taxpayers. And you want to throw  
20 your net into that sea, right?

21 A Yes. We want to get our offer in front of as many people as  
22 possible.

23 Q Okay. So there's TaxACT up there and here comes its net.  
24 We've got a big net down there (indicating). And you're hoping  
25 some taxpayers will climb into your net?

1 A Yes.

2 Q And one of the ways -- your strategy is free and then low  
3 cost and then quality. I don't mean to say in that order, but  
4 those are ways you attract people into your net, as I understand  
5 what we've been talking about, right?

6 A Yes.

7 Q All right. Then we've got, let's say, Block, and we can put  
8 Intuit in there too. And they have their net going into the  
9 same pool, right, same -- but they have got a different  
10 strategy.

11 What's their strategy? It's brand, correct?

12 A Yes.

13 Q What else do you think?

14 A They will differentiate based on features and quality of  
15 service.

16 Q All right. Quality.

17 A It's implied in their brand.

18 Q All right. So you're both going in the same sea. You just  
19 have different competitive strategies of how to get people in  
20 that net, right?

21 A Yes. We depend greatly on word-of-mouth advertising.

22 MR. WAYLAND: So I'm marking that as Trial Exhibit 6,  
23 your Honor.

24 (WHEREUPON, a certain document was marked Trial Exhibit 6  
25 for identification as of September 7, 2011.)

1 BY MR. WAYLAND:

2 Q Mr. Dunn, can a product ever be in both places at the same  
3 time, premium and value?

4 A It's a business model, not a product.

5 Q Not a product. All right. But there are products that go  
6 on either side of the category or am I misunderstanding?

7 A There are companies on each side of that list. You don't  
8 have to look any further than their home page to determine who  
9 is who.

10 Q Okay. With the Court's indulgence, I'll just remind you  
11 that I have questions. If you answer them directly, it will  
12 just be a lot quicker. And your counsel will have a chance to  
13 ask you questions and get out whatever you need to get out,  
14 okay.

15 MR. WAYLAND: Is that all right, your Honor?

16 THE COURT: It's fine. Proceed.

17 BY MR. WAYLAND:

18 Q All right. So let's go back and make sure I understand  
19 everything I need to understand about the value and premium  
20 distinction.

21 It's a business model in your mind. It's not a distinction  
22 between individual products, right?

23 A Correct.

24 Q So a company on the right side could be selling premium --  
25 could be selling premium products on the left side -- or could

1 be selling premium products?

2 A I don't believe so, no. You're either on one side or the  
3 other.

4 Q All right. Now, let's take a minute on assisted.

5 You believe sir, don't you, that the only likely reason that  
6 someone will switch from a TaxACT product to assisted is because  
7 somehow a loss of trust or life event?

8 A I believe I said there was a loss of confidence on the part  
9 of the taxpayer. An example of that would be a life event.

10 Q You're sure you said only an event as we've discussed  
11 before? That someone somehow -- loss of trust or life event,  
12 right?

13 A That's one reason why someone would leave tax software. And  
14 when they regain their confidence or that life event goes away,  
15 they might come back.

16 Q The Free File Alliance is a partnership between tax prep  
17 companies and the IRS, right?

18 A Yes.

19 Q And today both H&R Block and TaxACT offer free tax prep  
20 products through the IRS Web site, right?

21 A Yes.

22 Q And post-acquisition, you can't have both brands in the FFA,  
23 right?

24 A One company cannot have two products on the FFA.

25 Q And you think you'd probably have to take the TaxACT brand

1 down after the transaction?

2 A We'd have to look at the exact results of what's happening  
3 to the particular customers on both sides, which I haven't had  
4 full details to look at. But I would guess that, yes, we would  
5 take the TaxACT one down.

6 Q Now, when the Free File Alliance first began, TaxACT made  
7 its product available free to anyone with an adjusted gross  
8 income above a hundred thousand, right?

9 A That is the first offer that we made on the Free File  
10 Alliance in tax year 2000, yes.

11 Q And at that time, were you the only company that was  
12 offering the free filing at that income level?

13 A Yes.

14 Q And in the second year, you changed your offer to provide  
15 free for customers with adjusted gross income above 50,000,  
16 right?

17 A Actually, we changed that in the first year for the second  
18 peak. Then in 2003, we started the tax season with that same  
19 offer. 50,000 and above, yes.

20 Q When you talk about peak, what do you mean?

21 A Tax season has two -- is like a camel. It has two humps.  
22 There is a sustained processing peak around February 1st or  
23 February 15th as people receive their information documents.  
24 Then the volume will level off or lower and then level off  
25 throughout March.



1           And then the last day of the year is the busiest time of the  
2   day -- is the busiest time of the year. The absolute peak is on  
3   April 15th or 16th or 17th, whatever the filing date happens to  
4   be that year.

5   Q   Now, after TaxACT was offering it to the \$50,000 and above  
6   product, did other digital tax providers follow?

7   A   What was the question?

8   Q   Going back to when you had the strategy of providing free  
9   for its customers above \$50,000. You said that in the second  
10   year.

11   A   On the Free File Alliance.

12   Q   Other companies filed suit, right?

13   A   Yes. As we changed our offer, other companies changed their  
14   offers as well during the 2003 tax season. At that time, there  
15   wasn't a lot of restrictions on the FFA as to how frequently you  
16   could change your offer so there was a lot of movement.

17   Q   And you were the first company to offer free for all through  
18   the FFA, right?

19   A   Yes, we were.

20   Q   And then what happened after you did that? What's the  
21   sequence of events in the FFA?

22   A   After we offered free for everyone in 2003, in 2004, a lot  
23   of companies offered free for everyone on the FFA.

24   Q   And then the FFA changed, right?

25   A   Then the FFA -- the IRS changed the rules on the FFA, yes.

1 Q Do you have an understanding of how that came to pass?

2 A Slightly. I mean, during 2003 -- after the 2003 tax season,  
3 Intuit asked the Free File Alliance members that we should  
4 restrict offers, which I believe is probably not legal for that  
5 group to restrain trade.

6 Q You're in the right room for that argument, sir.

7 A So discussion on that stopped, and then after the 2004 tax  
8 season, the IRS decided to do that. How and why. You know, I  
9 asked them not to, but they did it.

10 Q And what was your response strategically, competitively  
11 after that happened?

12 A In 2005?

13 Q Yes.

14 A Yes, for 2005, we felt we really didn't have any option.  
15 Since so many companies had provided free products in 2004 on  
16 the Free File Alliance and they wouldn't necessarily be able to  
17 offer them there for 2005, we felt that we really had no choice  
18 but to be the first to do it there or perhaps at the same time  
19 as others.

20 Q I'm sorry. I just lost the end of that.

21 So what did you actually do? You offered free -- before  
22 your Web site?

23 A We offered free for everyone.

24 Q On your Web site?

25 A On our Web site.

1 Q And that was a first in the business, right?

2 A Well, a lot of companies had done it on the FFA in 2004, and  
3 as we contemplated what we were going to do for 2005, we  
4 certainly considered that any one of them might do it in 2005 as  
5 well. So yes, we felt that we really had no choice; that we  
6 needed to do that.

7 We also felt that the IRS was Walmarting us and that we  
8 needed to make a better offer on our Web site than we had on the  
9 IRS Web site so that customers would come to us, not to the  
10 IRS.gov.

11 Q It turned out you were pretty good businessmen. You said,  
12 hey, what's going to next and you said, well, maybe some people  
13 will go free. We better do it first. And you did it first and  
14 you beat everybody else to the market with your free Web site,  
15 right?

16 A Yes. As it turns out, no one else did follow that year.

17 Q You got a jumpstart, and that was a pretty good business  
18 decision, right?

19 A Yes, it worked out well for us.

20 Q And you've actually called that a watershed moment for the  
21 company, right?

22 A Yes. It was a watershed moment for the company and for the  
23 industry.

24 THE COURT: Can I just understand practically how this  
25 worked. So you were still on the FFA Web site?

1 THE WITNESS: Yes. The FFA changed their rules so that  
2 the FFA in aggregate would have to limit their offers to  
3 70 percent of the tax-paying population. And the IRS computes  
4 an AGI limit, and no one can make an offer that exceeds that  
5 AGI.

6 Individual companies can only make an offer on the Free  
7 File Alliance that appeals to 50 percent of the tax-paying  
8 public or less. And the idea that the IRS put out was that  
9 would foster competition by allowing differentiation on the FFA.

10 THE COURT: I got that part. So in 2005, on your Web  
11 site you're offering free federal filing for all. But on the  
12 FFA Web site, you were given a more cabined offer?

13 THE WITNESS: Yes. Our offer on the Free File Alliance  
14 would have been more capped. And honestly, I can't remember  
15 what the offer was that year. But the point was that prior to  
16 2005, the IRS had the Walmart supercenter of tax software  
17 offers. You had one site that had 18 offers, and they were the  
18 best you could find for any of those products on the Internet.

19 So here's an institution in the United States  
20 government that says they want to compete with the industry and  
21 if we don't provide free filing services, they will. So what  
22 were we doing as an industry? We were helping them build their  
23 Web site. We were making our best offers there, sending our  
24 customers -- sending customers there to find our offers. And so  
25 in 2005, one of the things that we considered in going free for

1 everyone on our site, besides the fact that others might do it,  
2 was the fact that we needed to have a better offer. The best  
3 offer we make needs to be on our Web site, not the IRS.gov.

4 MR. WAYLAND: Thank you, your Honor.

5 BY MR. WAYLAND:

6 Q Now, after you implemented your free-for-all Web site  
7 strategy, you saw an increase in the number of electronically  
8 filed returns that you processed, right?

9 A Yes.

10 Q Okay. Now, is it your -- part of your strategy to force any  
11 of the other competitors to try to offer free at all?

12 A I would have preferred if they hadn't.

13 Q Right. Did you think it would be helpful if you forced  
14 Intuit, for example, to have to offer a free product, compete  
15 with you on that level?

16 A No. I would have preferred to have the only free-for-all  
17 product out there for as long as I could have.

18 Q Let's look at Government Exhibit 2817. That's at Tab 13 in  
19 your book, sir.

20 These appear to be the notes or the minutes of a strategy  
21 meeting on January 22, 2008. You'll see among the attendees  
22 that are listed is Lance.

23 Any other Lances at the company?

24 A No.

25 Q Do you have any recollection of this meeting, sir?

1 A Specifically, no.

2 Q Did you attend strategy meetings from time to time?

3 A Infrequently.

4 Q But you do, right?

5 A Yes.

6 Q No reason to believe that you weren't there if you see your  
7 name on this?

8 A No. There is no reason to believe that I wasn't there for  
9 part of it.

10 Q If you go down, the third bullet has a heading, "Overall  
11 will be a difficult year for marketing and a difficult year to  
12 expand, et cetera."

13 And then there's some subpoints. And one of them says,  
14 "Look at the product. Redefine what is free. We need to better  
15 differentiate our free offer from that of TurboTax and raise the  
16 stakes so Turbo has to offer their free program to everyone  
17 rather than selectively marketing it."

18 Do you remember a discussion about that particular potential  
19 strategy?

20 A Yes. At this point, TurboTax had not rolled out  
21 aggressively free. They were selectively using it, for example,  
22 in search. So you could search for free tax software, and  
23 Intuit would have a free offer there next to ours.

24 But they did not have free as prominent on their advertising  
25 and their home page as they do today.

1 Q Why would it be helpful for you to raise the stakes so that  
2 Turbo has to offer their free to everyone? How does that  
3 benefit you?

4 A They stop just specifically targeting us, our free  
5 customers.

6 Q So this is a response to them targeting your customers?

7 A The way that they were implementing free was that they were  
8 only providing free products to people that were looking for  
9 free products. Which at that time we were the only ones out  
10 there suggesting and having a free product for everyone on our  
11 home page.

12 So at this point, they were selectively offering free, yes.

13 Q Which you saw as a threat to your customers, right?

14 A Not to our customers. At the end of the day, we really  
15 appeal to different customers. But confusion in the  
16 marketplace, yes, they're promoting free, we're promoting free,  
17 but at the end of the day, we're promoting free to try and get  
18 customers that are value conscious and cost conscious. They're  
19 promoting free to try and get people that are making their  
20 purchase decision on something other than just price.

21 Q And Intuit eventually did -- or TurboTax -- launch a free --  
22 a marketwide free, right?

23 A Eventually. I'm not sure they did it in 2008 or not.

24 Q Okay. And then H&R Block followed?

25 A They have more recently, yes. Free has universal appeal.

1 Q Got to get those fish in the pond.

2 A It's a big pond. You have to get your message out in front  
3 of as many people as possible.

4 Q You were the first company to use the phrase, "Free to  
5 prepare, free to print, free to E-file," right?

6 A Yes.

7 Q And then that phrase has been grabbed by some of your  
8 competitors?

9 A Yes.

10 Q Intuit grabbed that phrase?

11 A Pretty much everyone in the industry is using it today.

12 Q And were you concerned about other people using your same  
13 phrase?

14 A Yes. You know, it was a good marketing message. We would  
15 have preferred to have kept it, but other institutions ruled  
16 otherwise.

17 Q After the acquisition, I understand from the testimony that  
18 you're going to be the president -- or -- is the title president  
19 of the digital business?

20 A I believe so, yes.

21 Q Right. And you'll be reporting to whom, sir?

22 A I will be reporting to Bill Cobb.

23 Q He is the president of the overall business, H&R Block's  
24 business?

25 A I believe, yes, he is the CEO of H&R Block.



1 Q So he'll have responsibility -- bottom-line drive,  
2 profits-in-the-door responsibility -- for the premium side of  
3 the business as well as the value side that you'll be running,  
4 right?

5 A Yes. I will have responsibility for both, yes.

6 Q All right. And your plan is de-emphasize the marketing of  
7 H&R Block's free product; is that right?

8 A No.

9 Q You don't think that the emphasis for marketing a free  
10 product would be placed behind the TaxACT brand?

11 A The market changes every year. We have to react to what's  
12 currently being done.

13 Q All right. Well, a couple of months ago when you were  
14 deposed, did you have the view at that time, whatever the market  
15 was, that the emphasis for marketing a free product should be  
16 placed behind the TaxACT brand?

17 A Okay.

18 Q I think that's a yes. That was your view then?

19 A Yes.

20 Q All right. And that will be yet another change in strategy  
21 for H&R Block's digital, correct?

22 A What will be a change?

23 Q Change of de-emphasizing the free brand.

24 A No. I just said that we would continue the free brand.  
25 They already have one. It's already successful. I haven't seen

1 the numbers on how successful it is. All of that's happened  
2 after I talked to Block.

3 I haven't gotten any reverse due diligence regarding their  
4 free, but it looks like it's successful. I would want to  
5 continue that.

6 Q After the market followed in offering free, you needed to  
7 continue to differentiate your product, right? Harder to fish  
8 in the pond if you can't differentiate yourself, right?

9 A Yes. Differentiation is important to us.

10 Q And one of the ways that you can differentiate yourself is  
11 to improve your product, right?

12 A Yes.

13 Q And in the case of tax software, one of the ways that you  
14 improve the product is to offer more forms than other people  
15 that you cover, right?

16 A Yes.

17 Q Okay. And that was one of the strategies that you follow is  
18 to increase the number of forms to make your products more  
19 attractive, right?

20 A Yes. We added the rest of the federal forms that we did not  
21 currently -- that we did not support at that time so that we  
22 could make the marketing claim free for everyone because we want  
23 to get our product -- our message in front of everyone, our  
24 potential customers.

25 Q And when you did that, was H&R Block offering -- making the

1 same offer, free for everyone, all the filing?

2 A No one but TaxHawk, Free Tax USA has a similar offer.

3 Q Now, in the last tax season, you lost share in comparison to  
4 TurboTax and H&R Block, right?

5 A By some metrics, that's what some people say, yes. Again,  
6 by E-file, we were relatively flat.

7 Q One of the reasons in your view for that change was that  
8 they are spending a lot more money than you are on promotion?

9 A They are heavily promoting free. And our free message is  
10 not as differentiated as it could be, yes. Value customers are  
11 having a harder time finding us.

12 Q That's because of all the noise in the market that H&R Block  
13 and Intuit are making, right?

14 A Yes.

15 Q Now, speaking of marketing, there is intense competition  
16 between companies to get marketing space, right?

17 A Yes.

18 Q And tell us where -- when we say "marketing space," what are  
19 you looking for? Is it Web advertising? Where are you  
20 advertising?

21 A Web advertising is the most competitive. You know, for  
22 example, Yahoo.com home page is a popular place to advertise.  
23 So yes, we try to get space on Yahoo.

24 Q And who else is trying to get that space on Yahoo for  
25 digital tax preparation?

1 A For digital tax preparation?

2 Q Yes.

3 A I would say pretty much everybody in the space.

4 Q And you spend money to get space, right?

5 A Yes.

6 Q All right. Who is spending the most money?

7 A I believe Intuit pretty much smothers everybody.

8 Q You're bumping up to them constantly when you're trying to  
9 buy space?

10 A Yes. I think we're going to get shut out on Yahoo. I think  
11 Intuit is going to buy it lock, stock and barrel.

12 Q Do you think that's going to hurt your business?

13 A We're going to have to find other advertising venues to  
14 promote product to our value customers, yes.

15 Q If you don't, it will hurt your business, right?

16 A Yes.

17 Q Okay. You also compete against H&R Block for media space?

18 A We bump into them less, but yes. Everybody. We compete  
19 against a lot of people for media space, but inside the DIY  
20 software, yes, we bump up against Block, but Block advertises  
21 their assisted. During tax season, we bump up against  
22 Flowers.com a lot too.

23 Q But you don't worry about Flowers.com taking away any of  
24 your tax prep business, do you?

25 A In essence, they do. If we can't get our product promoted,

1 it is hurting us.

2 Q Where can I put flowers on that chart? Never mind.

3 A We bump up them again advertising. That was the question  
4 you were asking.

5 Q Do you monitor the prices that Intuit and H&R Block are  
6 charging for their products?

7 A Yes. We have to differentiate ourselves against them.

8 Q Let's look at Government Exhibit 28-20, which is at Tab 23  
9 in your book. This is a document, Mr. Dunn, that's titled  
10 "Price Increase Pros and Cons." On the left side, there's a  
11 series of pros. On the right side, a series of cons. And there  
12 seems to be a set of prices.

13 I think it refers to standard Deluxe 14.95, Deluxe 12.95 and  
14 is that ultra or ultra Deluxe, sir?

15 A Ultimate bundle. Combination of Deluxe and state.

16 Q Have you seen this document before?

17 A Only in my deposition.

18 Q Do you recall any discussions about whether or not you  
19 should be increasing your prices to the 14.95 level for  
20 standard?

21 A No, I don't.

22 Q Who has pricing authority at the company? Do you?

23 A Pardon?

24 Q Who has prizing company at the company?

25 A The four founders, but any price increase we'd have to take

1 to the board of directors as well.

2 Q You see the second bullet says, "The price increase will net  
3 additional resources while still maintaining an advantage in  
4 cost relative to our main competitors, Intuit and H&R Block."

5 Do you see that?

6 A Yes.

7 Q "We can still claim value leader."

8 Do you agree that you could still claim value leader if you  
9 raise your price to 14.95?

10 A I believe we could claim value leader. I think it would  
11 break our value proposition, but I'm sure we could claim it.

12 THE COURT: Mr. Wayland, I'm presuming from your  
13 questions that this is a TaxACT document.

14 MR. WAYLAND: I'm sorry, your Honor?

15 THE COURT: Is it a TaxACT document from any particular  
16 time period or year?

17 BY MR. WAYLAND:

18 Q Do you know, sir, when there was a discussion about raising  
19 your prices to 14.95, 12.95 and 17.95?

20 A No idea.

21 Q Do you know if you actually raised your price to 14.95 for  
22 the standard?

23 A Standard has never been changed. It's 9.95. Always has  
24 been.

25 Q Standard plus state, how much is that?

1 A Depends on the time of year, but generally, our state  
2 product runs about 16 to 17.95 as a stand alone with standard.

3 Q All right.

4 THE COURT: So we don't know when this document was  
5 created?

6 MR. WAYLAND: I don't think this witness knows enough  
7 about it.

8 THE COURT: That was becoming apparent to me.

9 BY MR. WAYLAND:

10 Q Do you know who Mike Larson is?

11 A Mike Larson is in charge of creative in our marketing  
12 department.

13 Q And what is creative? What's the responsibility of  
14 creative?

15 A He is responsible for creating advertising that runs on  
16 banners, e-mails, Internet. He is responsible for coming up  
17 with ideas for our advertising.

18 Q And how long has he been at the company?

19 A Mike has probably been there ten years.

20 Q All right. So he's pretty familiar with the business?

21 A He's familiar with his job.

22 Q All right. Well, part of his job is to market the business,  
23 right?

24 A His job is to come up with creatives and make our  
25 advertising stand out from others.

1 Q All right. Let's look at Exhibit 24. I'm sorry, Tab 24.  
2 The exhibit is Government Exhibit 28-32.

3 A I'm sorry. What tab?

4 Q Tab 24. This is a TaxACT brand analysis prepared by Mike  
5 Larson, June 4th, 2010.

6 You've seen it before?

7 A I saw this in my deposition.

8 Q All right. Do you recognize this as a document that would  
9 fall under Mike Larson's responsibility to prepare?

10 A Yes. As I said, he is responsible for creating advertising  
11 and, you know, differentiating our products from others that are  
12 being advertised.

13 Q All right. Would you look at the third page of the  
14 document. Do you see at the bottom of the page, there's a  
15 heading that says, "How Are the Major Direct competitors  
16 Positioning the Above Items?"

17 Do you see that?

18 A Yes.

19 Q And then underneath it, he lists two competitors, TurboTax  
20 and H&R Block, correct?

21 A Yes.

22 Q And if you turn the page, you'll see at the top, it says,  
23 "Our competitors have some branding advantages."

24 Do you see that?

25 A Yes.



1 Q And then the two competitors that he discusses are Turbo and  
2 H&R Block?

3 A Yes.

4 Q Okay. So the person whose principal responsibility is to  
5 come up with marketing campaigns for you has identified the  
6 major competitors as TurboTax and H&R Block, correct?

7 A These are two that will advertise their tax products a lot,  
8 yes.

9 Q All right. And if you -- just so there's no doubt about it,  
10 if you'd turn to the next page at the bottom under "Brand Audit  
11 Overview for Creative," you'll see that your -- under the No. 1,  
12 you'll see that your marketing fellow, says, "Major competitors  
13 refers to H&R Block At Home and TurboTax," correct?

14 A Yes.

15 Q And he's designing marketing strategies to compete with  
16 these major competitors, right?

17 A He comes up with ideas for creatives, yes, but that's not  
18 strategy. Anything he creates is going to be approved,  
19 disapproved, reviewed by the vice president of marketing, as  
20 well as Cammi Greif, the chief marketing officer.

21 THE COURT: Do you have any role in approving marketing  
22 plans or do you review them as a regular --

23 THE WITNESS: Only in the broadest sense. You know,  
24 Cammi and I and the four founders will discuss, you know,  
25 specifically how much the marketing budget is going to be.

1 Specifically, you know, big buys. Where we might be promoting.  
2 Whether we should by, you know, more premium space on Yahoo's  
3 home page or MSN's home page versus, you know, run of site,  
4 which is kind of a remnant buy.

5 So we talk about big issues. But in terms of, you  
6 know, specific execution of specific campaigns, no. That's  
7 handled by Kris Peterson, vice president of marketing.

8 BY MR. WAYLAND:

9 Q Before we leave the document, Mr. Dunn, if you look back on  
10 the prior page from where we were just looking at, the one that  
11 has, "Our competitors have some branding advantages." The Bates  
12 number at the bottom is 1262.

13 A 1262. Okay.

14 Q You'll see just above the last heading, there's a sentence  
15 that says, "Each company" -- and referring to TurboTax and H&R  
16 Block -- "puts an emphasis on a different point. Turbo is ease  
17 of use, H&R Block is on accuracy and we are on comprehensiveness  
18 and price."

19 Do you have any sense of in June of last year whether that's  
20 your understanding of what the companies were emphasizing?

21 A I'll take Mike's word for it. I'm sure he looked at the  
22 advertising copy for each much more closely than I would have.

23 Q Who is -- is it Cammi Greif?

24 A Cammi Greif.

25 Q What is her position?

1 A She is chief marketing officer and cofounder. She is one of  
2 my partners.

3 Q And what are her responsibilities at the company?

4 A Her primary responsibility is marketing, but like all of the  
5 four cofounders, we share in coming up with the vision and  
6 strategy of the company.

7 Q Now, Mr. Dunn, from time to time over the course of your  
8 involvement with 2nd Story, you have used financial advisors to  
9 seek investment or other access to capital, correct?

10 A We are currently owned by a private equity -- two-thirds  
11 owned by a private equity firm, which means that we are  
12 constantly for sale, yes.

13 Q And you know that from time to time, your company has  
14 prepared various offering memoranda describing the company and  
15 its business for use in that purpose, right?

16 A Yes.

17 Q And the information in those materials, generally you would  
18 expect to be accurate, right?

19 A Yes.

20 Q And you would generally be familiar with the information  
21 that was in those memoranda?

22 A Yes.

23 Q All right. Let's walk through several of them, sir. Let's  
24 start with Government Exhibit 28-8 which is at Tab 26 in your  
25 binder.

1           This document, Mr. Dunn, is entitled "Confidential  
2   Memorandum, 2nd Story Software." And it is prepared by the  
3   Greene Holcomb & Fisher company; is that right?

4   A   Yes.

5   Q   And I think it was about 2004, do you remember that, that  
6   this was prepared?

7   A   Sounds about right.

8   Q   If you look at the second page, there is an appendix, table  
9   of contents listing, and it says, "Fiscal 2003 audit and  
10   financial statements," indicating that they are attached.

11           So that would lead you to believe it's probably about 2004,  
12   right?

13   A   Yes.

14   Q   All right, sir. Let's look at page 2 of the document.

15           And this is a page that gives the company overview,  
16   correct?

17   A   Yes.

18   Q   And again, it's a familiar story if we look at the second  
19   paragraph. "2nd Story has rapidly gained market share and brand  
20   name recognition by offering a full-featured, tax-preparation  
21   product for use online," et cetera.

22           That's correct, right? That's your basic story?

23   A   Yes.

24   Q   All right. And --

25   A   It was in 2004.

1 Q Still is, right? It's still your story basically, isn't  
2 it?

3 A Yes.

4 Q And as you see, the last sentence says, "Prices for each of  
5 these products and services are considerably below its primary  
6 competitors."

7 So competitors who are offering at a higher price are Intuit  
8 and Block, generally, right?

9 A Yes. Those are premium products.

10 Q Let's turn to page 9 of the document.

11 Now, this, sir, under the heading "Industry Overview," has a  
12 chart, right? Sort of a flow chart, I guess, or a chart?

13 A Yes.

14 Q And so as I understand it, this chart is trying to break  
15 down the -- what happens on individual returns. Let me say it  
16 better.

17 Starting at the top with all the individual returns that are  
18 filed, right, the whole universe of filing?

19 A Right. That's our potential customer base, 132 million tax  
20 returns.

21 Q And then it breaks down on two wings. On the left wing, 54  
22 million self-prepared tax returns, correct?

23 A Yes.

24 Q And on the right wing, 78 million professionally prepared,  
25 right?

1 A Yes.

2 Q And then on the left, you go down under the self-prepared to  
3 31 million manually prepared.

4 We've been referring to that as pen and paper sometimes  
5 here, right?

6 A Yes.

7 Q And then 23 million using software, correct?

8 A Yes.

9 Q All right. And so if you're looking at the whole universe  
10 of people who are filing, you described the world as set forth  
11 in this chart, right? It's a fair way to think about everybody  
12 who is filing their taxes?

13 A Yes.

14 Q Are these all the fish in the ocean, or that's it, right?

15 A Yes. 132 million is it in 2004.

16 Q All right. And the digital market is the group that is the  
17 23 million using software, right?

18 A Yes.

19 Q All right. Then let's go to page 14.

20 And now we're talking about -- we're not talking about the  
21 universe as much anymore, but we're talking about more specific  
22 competition, correct?

23 A Yes.

24 Q Under this, it says, "The company's major competitors for  
25 both desktop and Internet-based income software and E-filing

1 services include Intuit and H&R Block," correct?

2 A Yes. Those are two other software providers.

3 Q And they are described as your major competitors, correct,  
4 in this?

5 A Certainly in the context of, you know, who this document was  
6 intended for, yes.

7 Q Why do you say that? Why would the people who get this want  
8 to know that Intuit and H&R Block are your primary major  
9 competitors?

10 A Where this document and others like it would have been sent  
11 to is to potential buyers. So this would have been sent -- a  
12 cover letter would have been slapped on it and sent to 30 or 40  
13 private equity firms.

14 And the first thing the private equity firm is going to do  
15 is say, "TaxACT sells tax software. I think Intuit sells tax  
16 software." And they'll go out and look at the public  
17 information available for Intuit. And so it would be -- you  
18 know, they're going to come -- or they're going to look at this  
19 in light of the information that they can get publicly  
20 available.

21 Q All right. Well, in the next paragraph you say, "Relative  
22 to its two major competitors, 2nd Story has positioned its  
23 product offerings as being of equal or higher quality and  
24 completely fulfilling the needs of a vast portion of the  
25 potential market. It also pursues a pricing strategy that

1 positions its products and services meaningfully below either  
2 Intuit or H&R Block, in some instances free," correct?

3 A Yes.

4 Q And that accurately described your strategy at the time,  
5 correct?

6 A Yes. It's clearly showing how we are different from Intuit  
7 and Block or from both of those. The reader of this document is  
8 going to come in with a bias that we provide software, they  
9 provide software, so how are we different than those?  
10 Especially with Intuit being an 800-pound gorilla, the reader of  
11 this is going to say, you know, why isn't Intuit potentially  
12 going to squash you like a bug?

13 So you know, one of the key points that this document is  
14 trying to make is that we serve different customers.

15 Q All right, sir. If you go to the next paragraph, it says,  
16 "Intuit is the recognized market leader and also the highest  
17 priced provider of similar products and services. H&R Block  
18 also enjoys very significant brand name recognition in part  
19 because of its nationwide strategy of storefront locations where  
20 tax professionals provide service."

21 So they have a branded product that -- they use your brand  
22 to help them sell their digital, right?

23 A Block has a strong brand, yes.

24 Q And the next paragraph says, "2nd Story believes its  
25 software and online products are equal or superior to either



1 those of Intuit and H&R Block and are offered to consumers at a  
2 lower price," correct?

3 A Yes.

4 Q So your view was your product was just as good, and the way  
5 you were going to get people to buy it was to sell at a lower  
6 price?

7 A Yes. We differentiate based on price. And the purpose of  
8 this document is to show the potential buyers that we service  
9 different customers than Intuit and Block. They are going to  
10 come up with the bias -- I mean, looking at even the companies  
11 today. Like I said, Intuit sells \$1.3 billion of consumer  
12 software today. We sell 70 million of consumer software. A  
13 potential buyer is going to say why doesn't Intuit squash you  
14 like a bug? Any time they want to they could do away with you.

15 The only way that we can show that we're not going to be  
16 squashed like a bug is to show how we're different than Intuit  
17 and Block and show how we serve different customers than Intuit  
18 and Block. And that's why we succeed and that's why we'll  
19 continue to succeed.

20 Q And it wasn't going to be relative to the people who invest  
21 in your company to know about those people on the right side of  
22 the column and the Free Tax and the TaxSlayers and the rest of  
23 the world?

24 A In 2004, that's barely getting started.

25 Q All right. A few years later, 2007, you had occasion to

1 engage Deutsche Bank for financial advice, correct?

2 A Yes.

3 Q All right. And again, their memorandum was prepared,  
4 correct?

5 A Yes.

6 Q And again, you would be familiar with the content of the  
7 document?

8 A Yes.

9 Q And you can see that. It's Government Exhibit No. 134 and  
10 it's at Tab 27.

11 And if you look, sir, at page 1 of the document, the No.  
12 1 -- it's the third page in, we're not going to -- if we read,  
13 we'll be reading the same thing mostly so we'll just skip  
14 through this pretty quickly.

15 Let's go to the next -- if you go to the bottom of that --  
16 the line that starts with, "Currently, the company generates a  
17 significant majority of its revenue by up-selling customers of  
18 its free tax preparation solutions to paid premium offerings,  
19 including state tax preparation with E-filing and deluxe  
20 versions with premium content."

21 Do you have a different view of what "premium" meant in this  
22 document than what we talked about earlier today?

23 A The content of our Deluxe program and our state program is  
24 at a price premium over our free product, yes.

25 Q Price premium. So now the word "premium" only means a

1 delta? It's a difference, premium; difference between our  
2 low-priced product and our high-priced product?

3 A It's a paid product so, yes, it is a different product than  
4 our standard product.

5 Q Why don't you call it your paid value offerings?

6 A That's not referring to a business model like premium versus  
7 over value here.

8 Q All right, sir.

9 A The price is still the same. State was probably 12.95,  
10 Deluxe was 9.95. That doesn't change our business model.

11 Q No. Just trying to understand why you're calling it what  
12 you're calling it, sir.

13 A "Paid" is the key word there.

14 Q But you added the word "premium." Somebody did.

15 A Yeah.

16 Q Okay. Let's go to page 16. This is under, again, the  
17 heading "Competition." Three years after the one we just saw.

18 You have market share of self-prepared, E-filed federal tax  
19 returns, correct?

20 A Yes.

21 Q All right. And then the second bullet point from the bottom  
22 says, "Competitors in the consumer tax preparation software  
23 market include CCH, H&R Block and Intuit."

24 Do you see that?

25 A Yes.

1 Q And CCH is not a big player, is it?

2 A Wolters Kluwer is a very big company.

3 Q In terms of their share of tax software, it's not very big,  
4 is it, on the digital side, consumer?

5 A It varies. They don't release their numbers. I don't know  
6 how big they are.

7 Q All right.

8 A And the point here is to compare ourselves with companies  
9 that have publicly available information. Compare and  
10 contrast.

11 Q Okay. Again, just quickly --

12 A To show how --

13 Q I'm sorry?

14 A We have to show how we can compete with big companies.

15 Q Again, just quickly on page 17, three years after the first  
16 memoranda we looked at, again, you're identifying your two main  
17 competitors as Intuit and H&R Block, right? Top of page 17.

18 A Yes. In the context of this document, I think that the  
19 readers would have information about them and would want to be  
20 how we compare to those. And like I said, this is the same  
21 thing. It's an offering memorandum. The potential investors  
22 want to know how we're not going to be smashed by a large  
23 company. So we have to show them how we are different and how  
24 we attract different customers.

25 So the point is the same. And I think if you read the

1 document as a whole, you'll see that that is one of the key  
2 points that this makes, as well as the management presentation  
3 that would logically follow after this.

4 Q All right, sir. Let's turn to another of the memorandum in  
5 the series, July 2009. This is Government Exhibit 28-24, and  
6 it's at Tab 29 of your book.

7 All right, sir. We're looking at Government Exhibit 28-24  
8 which is at Tab 29 in your book. And we'll look at page 3.

9 A Yes.

10 Q And sir, do you see in the second paragraph, again, you're  
11 describing yourself as an industry innovator in the delivery of  
12 free online tax software. And you've generated your own  
13 powerful brand affiliation, correct?

14 A That refers to the chain reaction, word of mouth, that I was  
15 referring to earlier, that's critical in value software.

16 Q Took you a while to build up that brand affiliation, word of  
17 mouth, right?

18 A It starts with the first unit.

19 Q And it gets better as you sell more units, more and more and  
20 more, right?

21 A I believe that that's how exponents work, yes. The more you  
22 have, the more referrals you get.

23 Q And you think it would take somebody 11 years to duplicate  
24 where you are now, right?

25 A No.

1 Q You thought that at your deposition?

2 A I believe that my deposition, I was asked how long it would  
3 take someone to get 11 years experience, and it would take 11  
4 years.

5 Q You were just being funny at the deposition?

6 A That was the question I was asked. That's the answer I  
7 gave.

8 Q Page 6. We're in the middle of the first paragraph, sir.

9 And we've pulled out, "Management believes the company's  
10 extensive domain expertise, combined with highly specialized  
11 tools and skills needed to develop a trusted tax preparation  
12 solution, provides a formidable barrier to competitive entry."

13 True when you put it out to the market then?

14 A Yes. I believe for someone to create a product from scratch  
15 would be difficult, but there are already 18 competitors out  
16 there.

17 Q But it's more than just loading up the software that allows  
18 you to have a program that makes you a successful company,  
19 right, sir?

20 A Correct. Like I said, starting in 1998, we created a very  
21 efficient and very effective software development and marketing  
22 infrastructure. And it's, I think, still the primary reason for  
23 this transaction. So yes, for someone to create that from  
24 scratch would be very difficult. We've had 20 years experience  
25 in tax software. I've had it with three different tax software

1 providers.

2 That is an asset that would be difficult to replicate. But  
3 there's a lot of players in the software market, and CCH will  
4 license a product to anybody.

5 Q Page 14, sir.

6 MR. WAYLAND: We're on page 14, your Honor, of  
7 Government Exhibit 28-24.

8 BY MR. WAYLAND:

9 Q In case the reader of the document missed the point the  
10 first time about barriers to entry, you've said it again.

11 "TaxACT has a large, loyal customer base and its  
12 differentiated product portfolio has built established,  
13 formidable barriers to entry, preventing other competitors from  
14 easily entering the tax preparation market with alternative free  
15 solutions."

16 You said it twice. Must have felt pretty strongly about it.

17 A Yes. I believe that it would be difficult for someone to  
18 build a product from scratch like we did, but there's plenty of  
19 other options out there. A lot of companies are doing it.

20 MR. WAYLAND: Your Honor, it's 5:30, right, your Honor?

21 THE COURT: I was planning on going until 5:00  
22 depending on where we are with the witness.

23 MR. WAYLAND: That's fine, your Honor. Just needed to  
24 know.

25 THE COURT: It's just 4:30.

1 MR. WAYLAND: Yes.

2 BY MR. WAYLAND:

3 Q Mr. Dunn, you use the concept backloaded when referring to  
4 maybe marketing in the business? "Backloaded," is that a term  
5 that means anything to you?

6 A I'm not familiar with the context.

7 Q All right. Let's look at Government Exhibit 952. That's at  
8 Tab 30 of your binder.

9 Mr. Dunn, this is what we've marked as Government 252. It's  
10 an e-mail from you to Todd Crockett.

11 Who is Todd Crockett?

12 A Todd Crockett is on our board of directors. He is managing  
13 partner at TA Associates.

14 Q And this is an e-mail from just this year in April 2011.  
15 And you write in the first paragraph, "I would normally  
16 anticipate that we would lose a little more share in the last  
17 two weeks as Intuit tends to be more backloaded than we are."

18 What does that mean?

19 A In this example or in this case, it means that they tend to  
20 have more returns filed on April 15th relative to their overall  
21 business.

22 Q All right. And why would that affect your share?

23 A In this context, we're talking about share of E-file units  
24 and using that as a metric for measuring our success this year,  
25 especially with respect to, you know, a potential sale.



1 Q Mr. Dunn, do you recall that TaxACT made some kind of  
2 marketing or business proposal to Fidelity at some point?

3 A No.

4 Q All right. Let me just see if I could refresh your  
5 recollection, and if not, we'll move on.

6 Let me show you what's been referred to as Government  
7 Exhibit 105. It's at Tab 50.

8 This is a document, sir, that's entitled "2007 Tax Season  
9 Proposal," submitted to Fidelity June 2007.

10 Do you recognize this at all?

11 A No.

12 Q Do you have any recollection of having anything to do  
13 with it?

14 A No.

15 Q All right. Okay. You can put it aside.

16 MR. WAYLAND: Give me a minute, your Honor. I may be  
17 done.

18 THE COURT: Certainly.

19 (Brief pause.)

20 MR. WAYLAND: Your Honor, we have a couple of documents  
21 that we have to close the courtroom. And that may be the way to  
22 end the day. Let me do a couple other ones before we do that.

23 THE COURT: Fine.

24 BY MR. WAYLAND:

25 Q Now, you, Mr. Dunn, in the day-to-day operations of TaxACT,

1 you monitor the prices of TurboTax and HRB? I think you told me  
2 that earlier.

3 A We do monitor them, yes.

4 Q All right. Let's look at Tab 34. This is a chart. It's  
5 Government Exhibit 28-29. And it's a chart that's entitled  
6 "2009 Competitive Price Comparison." And it's followed with  
7 some pages of product comparison as well.

8 Do you see that, sir?

9 THE COURT: Can I just correct you for a second. Are  
10 we on Tab 34?

11 MR. WAYLAND: Yes.

12 THE COURT: Is this Government Exhibit 19, not 29?

13 MR. WAYLAND: It's 28-19, your Honor.

14 THE COURT: Just for the record to be correct.

15 BY MR. WAYLAND:

16 Q Do you see, sir, on this 2009 Competitive Price Comparison  
17 that you're comparing the prices of TaxACT, H&R Block and  
18 TurboTax? Do you see that?

19 A I believe that's what this document does, yes.

20 Q And then the next page is a description of the competitive  
21 positioning statements for each of those three competitors,  
22 correct?

23 A Yes.

24 Q And then if you'd turn to two pages later, you'll see -- the  
25 Bates number is 91 at the bottom, sir. You'll see a 2009

1 features comparison that has TaxACT, H&R Block and TurboTax,  
2 correct?

3 A Yes.

4 Q Okay.

5 THE COURT: Mr. Wayland, just to slow you down for a  
6 second, so this is a TaxACT document?

7 MR. WAYLAND: It is, your Honor.

8 THE COURT: And Mr. Dunn, is this the kind of features  
9 and competitive price comparison that TaxACT does on a regular  
10 basis every year in preparation for every tax season?

11 THE WITNESS: No, not to my knowledge.

12 THE COURT: Was this only done in 2009?

13 THE WITNESS: I'm not familiar with this, but this is  
14 not something that we do in the ordinary course of business.

15 THE COURT: Okay.

16 MR. WAYLAND: All right, your Honor. We need to close  
17 the courtroom now.

18 THE COURT: Could I just ask you how long do you  
19 estimate the closed session for Mr. Dunn will be?

20 MR. WAYLAND: Should be relatively short, your Honor.  
21 I just have a couple of documents to go through. It will take  
22 us to 5:00. I think I should be done at the end of the day.

23 THE COURT: Frankly, if we can finish the closed  
24 session for Mr. Dunn today so that we start at 9:30 with the  
25 open cross, I'd like to do that. But I guess you can't tell me

1     how long you're going to be on cross of the --

2             MR. WAYLAND:   It may take me a little bit longer than  
3     that anyway, your Honor.  It really depends on how long it takes  
4     us to get through the documents.

5             MR. ROBERTSON:  Your Honor, the witness will be on for  
6     quite a bit longer because we also have our direct that we will  
7     put on with Mr. Dunn as well, which also may include  
8     confidential documents.  So there's no chance we're going to get  
9     through with the confidential section of that today.

10            THE COURT:  Okay.  All right.  Let's close the  
11     courtroom, and we'll conclude with the direct examination with  
12     the government's closed documents.  We'll start tomorrow then at  
13     9:30 with cross-examination of these closed documents or would  
14     you just prefer to wait and deal with cross-examination of these  
15     documents --

16            MR. ROBERTSON:  I may have other confidential  
17     documents.  It might make sense to wait, and I'll do it at the  
18     end.  And that way counsel can redirect, and we can recross and  
19     tidy that up.  I think that will make it cleaner.

20            THE COURT:  All right.

21            MR. ROBERTSON:  Otherwise, we may have people trying to  
22     get in at 9:30 and that would be a little clumsy.

23            THE COURT:  Right.  I was thinking that we might be  
24     able to avoid that.  It's clear we're going to have at least one  
25     more closed session with Mr. Dunn so we'll start 9:30 with an

1 open courtroom, but we will now close it to at least do these  
2 documents.

3 MR. WAYLAND: Thank you, your Honor.

4 THE COURT: Okay. We have now closed the courtroom.  
5 This portion of the transcript will be sealed. I want to  
6 confirm with counsel that the only people remaining in the  
7 courtroom are appropriate to be here.

8 MR. WAYLAND: Yes, your Honor, for the government.

9 THE COURT: Mr. Robertson?

10 MR. ROBERTSON: Yes, your Honor.

11 THE COURT: Thank you, Mr. Robertson. Please proceed,  
12 Mr. Wayland.

13 MR. WAYLAND: Thank you, your Honor.

14 CROSS-EXAMINATION

15 BY MR. WAYLAND:

16 Q Mr. Dunn, do you who know Leigh Aragon and Greg  
17 Hollingsworth?

18 A They are in our marketing department.

19 Q And what responsibilities do they have?

20 A Leigh Aragon does preliminary negotiation with potential  
21 partners as sort of an outside liaison as she also does PR.

22 Q And Greg Hollingsworth?

23 A He is no longer with the company, but when he was with the  
24 company, he was in our social media.

25 Q And what was his responsibility there?

1 A He would respond to Facebook postings and Twitter. Did what  
2 I would consider almost technical support.

3 Q All right, sir. Let's look at Tab 49. This is a document  
4 entitled "Competitive Analysis Tax Year 2009," created by Leigh  
5 Aragon and Greg Hollingsworth.

6 A Okay.

7 Q Turn to the introductory page, which has the Bates number  
8 that ends 666 on it.

9 A Yes.

10 Q And you'll see that the middle paragraph says, "Our focus  
11 this season was on differentiating our free product from that of  
12 our competitors." And then on the right-hand side, they have  
13 listed TaxACT, H&R Block and TurboTax, correct?

14 A Yes.

15 Q All right, sir. On a page we've shown, Mr. Dunn, it says,  
16 "Upstream traffic sources: HRBlock.com."

17 Do you see that?

18 A Yes.

19 Q And you'll see that this apparently is tracking where your  
20 business -- or what hits on various Web sites and et cetera,  
21 correct?

22 A Yes.

23 Q I shouldn't say "et cetera," but it's on sites -- media  
24 sites like Facebook, MySpace and YouTube, correct?

25 A I believe it has a lot of Web sites here, yes; Google,

1 Yahoo, Microsoft, yes. It has a lot of sites.

2 Q All right. And then in the chart on the right side, there  
3 are Google, Yahoo, Microsoft, Facebook are listed, and then the  
4 three companies TaxACT, H&R Block and TurboTax with percentages.

5 Why is it important to know what kind of traffic you're  
6 getting at these various sites?

7 A We utilize it to determine where we should advertise.

8 Q All right. And how do you utilize it? What do you want to  
9 know in order to make your decisions to advertise?

10 A Whether, you know, some of those 140 million taxpayers are  
11 going to Google, Yahoo, IRS, Facebook, Microsoft.

12 Q All right. And then you see at the bottom, it says that,  
13 "H&R Block received more of its traffic from IRS.gov than any of  
14 the three big and drew a rather significant chunk of traffic  
15 from social media sites like Facebook, MySpace and YouTube.  
16 These three sites combined account for a certain percentage of  
17 upstream traffic."

18 What would you do with this kind of information? Make  
19 decisions about media buys or advertising?

20 A It would be helpful there but, you know, it just -- it  
21 generally kind of confirms, I think, probably what we already  
22 know about, you know, where taxpayers go to find information.

23 Q All right. Let's just go to the next document. Before I  
24 show you that document, let's set the stage.

25 Now, you sell online product, correct, Mr. Dunn, online

1 product? And you also sell software in a box, right?

2 A This year we sell software in a box for the first time in a  
3 long time.

4 Q And that's new, right?

5 A It's been a while since we've -- anyone's bothered to take  
6 our product to retail, yes.

7 Q And how long has it been since anyone bothered to take your  
8 product to retail?

9 A I don't remember specifically. It was probably 2004.

10 Q All right. And where is your product going to retail now?

11 A Where is it going to retail now?

12 Q Yeah.

13 A I believe Avanquest had it at Staples this past tax  
14 season.

15 Q What is Avanquest?

16 A It is a software distributor.

17 Q And do you have an arrangement with Avanquest to distribute  
18 your software?

19 A We have a contract with Avanquest I would say much like a  
20 license agreement.

21 Q And how does that work? What's the basic business  
22 proposition?

23 A We give them a product, they give us a royalty and they sell  
24 it.

25 Q And so it's their responsibility to go out to the retailer



1 and market it and put it on the shelf?

2 A Yes. If that's what they want to do with it.

3 Q All right. And in November of 2010, your product was  
4 offered for the first time at Staples?

5 A In a long time.

6 Q And who else was being sold at Staples? Do you know?

7 A I believe this past tax season Intuit and Block were.

8 Q And what was your value proposition to get in the door?  
9 What was your selling proposition?

10 A You know, that was really up to Avanquest, but I believe  
11 they had a slightly lower price than Block and Intuit's.

12 Q And were you familiar with any of the marketing materials  
13 that Avanquest prepared in connection with this business  
14 proposition?

15 A No.

16 Q All right. So you haven't seen or reviewed any of  
17 Avanquest's materials?

18 A No. I believe Kris Peterson, I think she has the right to  
19 review it, but that's primarily for accuracy because we have to  
20 provide the technical support for this product on the back end.  
21 We don't want them saying something about the product that we  
22 don't do.

23 Q Let me show you what we've marked as Government Exhibit 62,  
24 which is at Tab 36 in your binder. Government Exhibit 63. I'm  
25 sorry. It's at Tab 36.

1           THE COURT: Can I just clarify for the record since  
2 it's my preference not to have closed sessions of a public  
3 trial, so was there something -- so Tab 49 and what we just  
4 looked at, it was necessary to do this in a closed session?

5           MR. WAYLAND: According to the defendants, your Honor.  
6 We didn't --

7           THE COURT: To seal the transcript for that?

8           MR. ROBERTSON: Your Honor, that document as well as  
9 the current one are third-party documents. They are not TaxACT  
10 documents. And those third parties had --

11          MR. WAYLAND: No. It was a TaxACT document.

12          MR. ROBERTSON: Which one?

13          MR. WAYLAND: This one.

14          THE COURT: I just want to be clear in my own mind. So  
15 Government Exhibit 104, which is at Tab 49.

16          MR. WAYLAND: Yes, your Honor.

17          THE COURT: Looks like a slide show created by two  
18 employees of TaxACT, Leigh Aragon and Greg Hollingsworth.

19          MR. WAYLAND: That's exactly correct, your Honor.

20          THE COURT: So hence, my question of why this part of  
21 the hearing had to be sealed and done in a closed courtroom.

22          MR. ROBERTSON: Your Honor, can I just check for a  
23 moment?

24          THE COURT: Yes.

25          (Brief pause.)

1 MR. ROBERTSON: We could -- your Honor, on the document  
2 that you're referring to right now, there are some pages in here  
3 that are competitively sensitive, but we believe that what was  
4 put up on the screen you could put back in the public record.  
5 We could try to clear that up later if your Honor wants us to go  
6 back and change the transcript.

7 THE COURT: Yes. And I think so far the only thing  
8 we've covered in the sealed part of this record has to do with  
9 Tab 49.

10 MR. ROBERTSON: Correct. And I was mistaken. I was  
11 looking at the one on the screen here, which is a different  
12 document.

13 THE COURT: Exactly. So I think at this point we can  
14 unseal the record up to this point. And if -- you know, it's  
15 hard to -- the minute we've sealed the courtroom, it's hard to  
16 redo this in a public forum. But let's be very careful before  
17 we seal the courtroom to make sure we're sealing it in talking  
18 about things that have to be done in a sealed context.

19 So the record is unsealed up to now. We are now on  
20 Government Exhibit 62. And this appears to be a --

21 MR. ROBERTSON: This is a document from Avanquest.

22 THE COURT: This is a document with Avanquest.

23 MR. WAYLAND: But was produced from the files of 2nd  
24 Story. That's because it's an agreement between 2nd -- proposal  
25 to 2nd Story. So I don't know why it would be sealed.

1 THE COURT: Mr. Dunn, do you have a confidentiality  
2 agreement with Avanquest?

3 THE WITNESS: Yes.

4 THE COURT: That requires you to keep confidential  
5 information that's related to your license agreement with  
6 Avanquest?

7 THE WITNESS: Yes.

8 THE COURT: Okay. So I think it is appropriate to seal  
9 the record from here on out as we discuss Government Exhibit 62.

10 MR. WAYLAND: Thank you, your Honor.

11 (The following portions, pages 122-123, were designated as  
12 confidential/attorneys' eyes only and sealed under a  
13 separate transcript per order of the Court.)  
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CERTIFICATE OF OFFICIAL COURT REPORTER

I, Lisa S. Schwam, certify that the foregoing is a  
correct transcript from the record of proceedings in the  
above-entitled matter.

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SIGNATURE OF COURT REPORTER

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DATE